

Message Text

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C O N F I D E N T I A L STATE 046254

FOR RALPH BRYANT, HOTEL CRILLON

TUESDAY, MARCH 13, 1973

HERSEY COMMENTS AS FOLLOWS: EURODOLLARS

REGARDING IMMEDIATE MEASURES RAISING EURODOLLAR INTEREST RATES, SEE HERSEY PAGES THREE AND FOUR. TOTAL INTERBANK OUTFLOWS PAGE FOUR REVISED TO 3.7 FOR FIVE WEEKS TO FEBRUARY 28. LOANS UP 1.4. LIABILITIES DOWN 2.3, OF WHICH 1.0 TO BRANCHES ABROAD AND 1.2 FROM AGENCIES AND BRANCHES IN NEW YORK. OF THE LATTER, 0.8 CANADIANS, 0.3 JAPANESE. WHETHER OR NOT MUCH OF THIS ASSOCIATED WITH TIGHT EUROMARKET, CLEARLY OUTFLOWS OF 3.7 CONTRIBUTED IMPORTANTLY TO THE PART OF 9.4 OFFICIAL SETTLEMENTS DEFICIT IN THE FIVE WEEKS NOT DUE TO UNDERLYING DEFICIT. BUT PICTURE VERY DIFFERENT IN WEEK ENDED MARCH 7, WHEN OFFICIAL SETTLEMENTS 4.3. INTERBANK LOANS UP CONSIDERABLY-- NEW YORK 0.3, OTHERS NOT YET KNOWN BUT GUESS SIMILARY AMOUNT-- BUT LIABILITIES UP REPEAT UP 0.3, OF WHICH 0.7 TO BRANCHES ABROAD WHILE FURTHER DECREASE 0.15 IN LIABILITIES OF AGENCIES AND BRANCHES IN NEW YORK AND DECREASE 0.3 IN OTHER LIABILITIES TO FOREIGN BANKS.

EXCELLENT LARRE PAPER DOWNPLAYS ROLE OF EURO- CURRENCY IN EXCHANGE MARKET INSTABILITY. STATES ON PAGE 27 THAT EUROMARKET NOT A POOL OF IDLE FUNDS. WHEN NEW DEMANDS ARISE
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BANKS MUST MAINLY SEEK NEW FUNDS.

THERE FOLLOWS MEMO ON FLOATING PREPARED BY MR. TRUMAN.
WHAT IS THE OBJECTIVE OF FLOATING? TO ALLOW EXCHANGE RATE TO
FOSTER ADJUSTMENT? TO DISCOURAGE SPECULATION LEST LIQUIDITY
FLOW IN AND/ OR LEST THEIR CURRENCY APPRECIATE TOO MUCH? IN
EITHER CASE:(1) CONTINUED UNDERLYING US DEFICIT WILL FORCE SOME
RATE MOVEMENT IF NOT OFFSET BY INTERVENTION OR CAPITAL FLOW
TO US; (2) US SHOULD AGREE TO SUBSEQUENT REVERSAL AS FAR AS
FEBRUARY- MARCH LEVEL; (3) FLOATS SHOULD BE INDEFINITE AND AVOID
PREMATURE FIXING. INTERNATIONAL SCRUTINY OF ANY NEW FIXED
RATES. STAFF UNCERTAIN ABOUT OBJECTIVES IN FLOATS. IS AIM
TO FLOAT WITHOUT MOVING? SINCE OBJECTIVES NOT UNANIMOUS, RULES
MAY BE IRRELEVANT. CONSULTATION AND AGREEMENT ON PRINCIPLES
MORE IMPORTANT THAN RULES.

ON RULES FOR FLOATING, SEE EMT NOTE PAGE 7 IF OBJECTIVE IS
SMOOTHING. SUGGEST ON RULES: (A) TREAT RESERVES OF SNAKE
COUNTRIES ON A NET BASIS TO REDUCE COMPLICATIONS OF
INTRA - SNAKE CREDITS. (B) EXAMPLE OF BASIC RULE; MAXIMUM
OF DOLS 80 MILLION INTERVENTION-- - CHANGE IN NET RESERVES--
INRESPONSE TO EACH QUARTER- PERCENT RATE CHANGE VERSUS DOLLAR FOR
COUNTRY AT LIMIT OF SNAKE; NORMALIZE ON FEBRUARY- MARCH CENTRAL
RATES. ALTERNATIVE OF DOLS10 MILLION PER THIRTY- SECOND.
LATTER FORMULATION IS ROUGHLY COMPARABLE WITH PRESENT
CANADIAN PRACTICE. (C) IF SNAKE WORRIED ABOUT
OTHER FLOATERS, APPLY RULE TO OTHERS USING SAME RELATIVE RATE
CHANGE AS KEY WITH MAXIMUM INTERVENTION SCALED BY SHARE IN
WORLD TRADE? AIM TO REDUCE CROSS RATE CONTROVERSIES. SAME
PROCEDURE FOR SNAKE DROP OUTS. (D) POSSIBLE SIDE CONDITION:
UNLIMITED INTERVENTION AFTER TWO PERCENT CHANGE IN WEEK, FIVE
PERCENT CHANGE IN MONTH. IS AGREEMENT POSSIBLE ON MAXIMUM
TOLERABLE OVERALL RATE CHANGES? (E) EXCEPTIONAL INTERVENTION
POSSIBLE FOR AGREED SPECIAL TRANSACTIONS LIKE ROYALTY PAYMENTS.
(F) INCLUDE NON- MARKET RESERVE CHANGES PRORATED OVER TIME ALONG
WITH INTERVENTION RESERVE CHANGES. AIM TO PREVENT ABUSE IN
USE OF NON- MARKET TRANSACTIONS. NOTE FRG RESERVES DECREASED
3.6 BILLION DM MID- JULY TO END- NOVEMBER 1972 DOE TO NON- MARKET
TRANSACTION; SAID TO BE TYPICAL. (G) SYMMETRICAL RULES FOR
UP AND DOWN TO FOSTER NO NET RESERVE CHANGE WHEN RATE RETURNS
TO A PREVIOUS LEVEL. AT FEBRUARY- MARCH FLOOR MAY WANT TO SUSPEND
RULES TO PERMIT DISGORGING OF DOLLARS. (H) OTHERWISE PERMIT
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RATES TO GO BELOW FEBRUARY- MARCH FLOOR IF COUNTRY FOLLOWS

RULES. BUT ANY NEW FIXED PARITY MUST RECEIVE INTERNATIONAL
APPROVAL. END. ROGERS

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